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Release 2013/12/18 :

CIA-RDP90G01353R000800020010-5

CONTROL NO. _____

CROSS REF: _____

PRIOR PAPERS ON THIS SUBJECT: ☒ NO ☐ YES

PRIOR CORRES SENT TO: _____

OTHER COMMENTS: *DD, Cy H/c*

by



107 JUL 1988

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EXECUTIVE REGISTRY FILE NO: **L-232-IR**

CROSS REF: _____

~~*Butler, W. R.*~~

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ROUTING SLIP

TO:

		ACTION	INFO	DATE	INITIAL
1	DCI				
2	DDCI		X		
3	EXDIR				
4	D/ICS				
5	DDI	X			
6	DDA				
7	DDO				
8	DDS&T				
9	Chm/NIC		X		
10	GC				
11	IG				
12	Compt				
13	D/OCA				
14	D/PAO				
15	D/PERS				
16	D/Ex Staff				
17	NIO/USSR		X		
18	D/SOVA/DI		X		
19	NIO/ECON		X		
20	ER				
21					
22					
SUSPENSE		20 Jul 88 Date			

Remarks To # 5: Please prepare coordinated response for DDCI signature.

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Executive Secretary

6 Jul 88

Date

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Before I dissem, does
this tasking suffice?

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to summary
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Executive Registry

88-2675X



THE ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D. C. 20301-2400

INTERNATIONAL
SECURITY AFFAIRS

02 JUL 1988

MEMORANDUM FOR ROBERT GATES

SUBJECT: Soviet Financial Balance Sheet

(S) We believe it is time for a fresh look at the Soviet economic dilemma and the pressures it is placing on Mikhail Gorbachev for changes in Soviet foreign policy or resource allocations to the military. Gorbachev's unprecedented attacks on the bureaucrats at the party conference reinforce our view that the economy continues to sputter and the reforms are bogging down.

(S) The Soviet economy is suffering due to economic mismanagement, massive spending on military modernization and the client states, and the dislocations created by Perestroika. The USSR is also afflicted by deteriorating terms of trade with the West as oil earnings have declined while imports have become much more expensive. Pressures on the Soviet economy are unlikely to abate in the near term, meaning that Gorbachev may be forced to choose soon between priorities that could affect U.S. interests for better or worse.

(S) One of Gorbachev's immediate problems is the shortage of hard currency in the Soviet economy. He will be presented with three unpalatable alternatives if hard currency earnings fail to rise:

- ° He can continue the reductions in Western machinery imports at the cost of economic efficiency and popular support for Perestroika (The Soviet machine building industry is falling far below output targets and has become a major bottleneck).
- ° He can step up borrowing in Western capital markets, which leaves the Soviets open to the potential use of political leverage by the West.
- ° Or, the Soviets could scale back on active measures and other low-intensity conflict operations in the West and the hard currency support (or its equivalent) provided to Cuba, Nicaragua, Vietnam and other clients.

Regardless of what choices are made, all decisions to spend hard currency under these circumstances are made more painful.

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(S) The U.S. has an obvious interest in how Gorbachev responds to his hard currency crunch. His choices may present us with opportunities to further the settlement of regional disputes or advance the cause of human rights. In order to shape policy we need a new, comprehensive analysis of the USSR's financial balance sheet--the sources of hard currency earnings and the drain on those earnings by imports, debt service and, most of all, the hard currency support for client states, active measures campaigns in the West, and all other programs requiring expenditures of hard currencies. The latter should include the approximate total hard currency costs of KGB and GRU operations, payments to front groups, the costs of sponsoring conferences, payments for publicity, travel expenses, technology theft activities, etc.

(S) A recent study completed by Rand estimated the USSR's total hard currency outlays on the Soviet empire alone to run at \$15-20 billion annually, which is an enormous amount that is not being met by Soviet hard currency earnings (around \$30 billion annually) given the need to service debt and pay for imports. We need to know if the Rand estimates are even in the ballpark. If they are, the Soviet "empire" could become even more of a drag on Soviet resources and helps explain why they are at least talking to us about settling the regional disputes. We tend to think the Soviets would show more willingness to cut their losses in the Third World than to sacrifice their military buildup or Perestroika. CIA's views on this would be greatly appreciated.



RICHARD L. ARMITAGE
Assistant Secretary of Defense
(International Security Affairs)

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